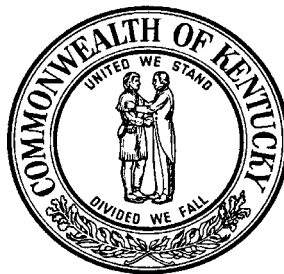


**LETTER FROM THE AUDITOR OF PUBLIC ACCOUNTS  
TRANSPORTATION CABINET**

**In Reference to the Statewide Single Audit  
of the Commonwealth of Kentucky**

**For the Year Ended June 30, 2004**



**CRIT LUALLEN  
AUDITOR OF PUBLIC ACCOUNTS  
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CRIT LUALLEN  
AUDITOR OF PUBLIC ACCOUNTS

Bill Nighbert, Acting Secretary  
Transportation Cabinet

**MANAGEMENT LETTER**

Pursuant to KRS 43.090 (1), which states, "[i]mmediately upon completion of each audit and investigation, except those provided for in KRS 43.070, the Auditor shall prepare a report of his findings and recommendations," we are providing this letter to the Transportation Cabinet to comply with KRS 43.090.

This letter presents the results of the work performed at the Transportation Cabinet, as part of our annual audit of the Commonwealth of Kentucky's financial statements.

In planning and performing our audit of the basic financial statements of the Commonwealth for the year ended June 30, 2004, we considered the Transportation Cabinet's internal control in order to determine our auditing procedures for the purpose of expressing an opinion on the financial statements and not to provide assurance on internal control. However, we noted certain matters involving the internal control and its operation that we considered to be reportable conditions under standards established by the American Institute of Certified Public Accountants. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of internal control that, in our judgment, could adversely affect the Transportation Cabinet's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and would not necessarily disclose all matters that might be reportable conditions. In addition, because of inherent limitations in internal control, errors or fraud may occur and not be detected by such controls.

As part of our audit of the Commonwealth's basic financial statements, we also performed tests of the Transportation Cabinet's compliance with certain provisions of laws, regulations, contracts, and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. The results of those tests disclosed instances of noncompliance that are required to be reported under *Government Auditing Standards*.



Bill Nighbert, Acting Secretary  
Transportation Cabinet  
(Continued)

Some findings are Other Matters that we have included in this letter to communicate with management in accordance with *Government Auditing Standards*.

Included in this letter are the following:

- ◆ Acronym List
- ◆ Findings and Recommendations (Reportable Conditions, Noncompliance, and Other Matters)
- ◆ Summary Schedule of Prior Year Audit Findings

We have issued our Statewide Single Audit of the Commonwealth of Kentucky that contains the Transportation Cabinet's findings, as well as those of other agencies of the Commonwealth. This report can be viewed on our website at [www.auditor.ky.gov](http://www.auditor.ky.gov).

This letter is intended solely for the information and use of management and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Crit Luallen", with a stylized flourish at the end.

Crit Luallen  
Auditor of Public Accounts

February 28, 2005



CRIT LUALLEN  
AUDITOR OF PUBLIC ACCOUNTS

Bill Nighbert, Acting Secretary  
Transportation Cabinet

**MANAGEMENT LETTER**

Pursuant to KRS 43.090 (1), which states, "[i]mmediately upon completion of each audit and investigation, except those provided for in KRS 43.070, the Auditor shall prepare a report of his findings and recommendations," we are providing this letter to the Transportation Cabinet to comply with KRS 43.090.

This letter presents the results of the work performed at the Transportation Cabinet, as part of our annual Statewide Single Audit of the Commonwealth of Kentucky.

In planning and performing our audit over compliance with requirements applicable to major federal programs, for the year ended June 30, 2004, we considered the Transportation Cabinet's internal control in order to determine our auditing procedures for the purpose of expressing an opinion on compliance with requirements applicable to each major federal program and to report on internal control over compliance in accordance with Office of Management and Budget (OMB) Circular A-133 and on the Schedule of Expenditure of Federal Awards (SEFA).

We noted certain instances of noncompliance with requirements applicable to major federal programs we considered to be reportable under standards established by OMB Circular A-133.

We noted certain matters involving internal control over compliance and its operation that we considered to be reportable conditions under standards established by the American Institute of Certified Public Accountants. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of internal control over compliance that, in our judgment, could adversely affect the Transportation Cabinet's ability to administer a major federal program in accordance with the applicable requirements of OMB Circular A-133.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and would not necessarily disclose all matters that might be reportable conditions.



Bill Nighbert, Acting Secretary  
Transportation Cabinet  
(Continued)

In addition, because of inherent limitations in internal control, errors or fraud may occur and not be detected by such controls.

As part of our audit of the Commonwealth's basic financial statements, we also performed tests of the Transportation Cabinet's compliance with certain provisions of laws, regulations, contracts, and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. The results of those tests disclosed instances of noncompliance that are required to be reported under *Government Auditing Standards*.

Some findings are Other Matters that we have included in this letter to communicate with management in accordance with auditing standards generally accepted in the United States of America and *Government Auditing Standards*.

Included in this letter are the following:

- ◆ Acronym List
- ◆ Schedule of Expenditures of Federal Awards
- ◆ Notes to the Schedule of Expenditures of Federal Awards
- ◆ Findings and Recommendations (Reportable Conditions)
- ◆ Summary Schedule of Prior Year Audit Findings

We have issued our Statewide Single Audit of the Commonwealth of Kentucky that contains the Transportation Cabinet's findings, as well as those of other agencies of the Commonwealth. This report can be viewed on our website at [www.auditor.ky.gov](http://www.auditor.ky.gov).

This letter is intended solely for the information and use of management and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Respectfully submitted,



Crit Luallen  
Auditor of Public Accounts

February 28, 2005



**LIST OF ABBREVIATIONS/ACRONYMS**

APA	Auditor of Public Accounts
BMS	Bridge Maintenance System
CFDA	Catalog of Federal Domestic Assistance
CFR	Code of Federal Regulations
DoS	Denial of Service
DOT	Department of Transportation
DMZ	Demilitarized Zone
FFY	Federal Fiscal Year
FHWA	Federal Highway Administration
FTA	Federal Transit Administration
FTP	File Transfer Protocol
FY	Fiscal Year
GOT	Governors Office of Technology
HIS	Highway Information System
JVB	Journal Voucher
KRS	Kentucky Revised Statutes
KBIS	Kentucky Bridge Information System
KyBMS	Kentucky Bridge Maintenance System
MARS	Management Administrative Reporting System
NBIS	National Bridge Information System
NCGA	National Council of Governmental Accounting
OIG	Office of Inspector General
OMB	United States Office of Management and Budget
OMS	Operations Management System
PMS	Pavement Management System
SEFA	Schedule of Expenditures of Federal Awards
SFY	State Fiscal Year
SMTP	Simple Mail Transfer Protocol
TC	Transportation Cabinet
U.S.	United States
XXS	Cross Site Scripting

**SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS**  
**FOR THE YEAR ENDED JUNE 30, 2004**

CFDA #	Program Title	Expenditures		Provided to Subrecipient
		Cash	Noncash	
<u>U.S. Department of Justice</u>				
Direct Program:				
16.728	Drug Prevention Program	\$ 38,756		
<u>U.S. Department of Transportation</u>				
Direct Programs:				
Highway Planning and Construction Cluster:				
20.205	Highway Planning and Construction (Note 2 ) (Note 3)	466,540,160		392,925
20.218	National Motor Carrier Safety	3,954,629		52,531
20.505	Federal Transit-Metropolitan Planning Grants	366,412		312,430
Federal Transit Cluster:				
20.500	Federal Transit - Capital Investment Grants	14,280,733		14,280,733
20.509	Formula Grants for Other Than Urbanized Areas	7,250,998		6,658,742
20.513	Capital Assistance Program for Elderly Persons and Persons with Disabilities	1,744,495		1,719,495
Passed Through From Military Affairs:				
97.004	State Domestic Preparednes Equipment Support	7,678		
97.036	Public Assistance Grants	5,981,171		
TOTAL TRANSPORTATION CABINET		\$500,165,032	\$ -	23,416,856

**NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS**  
**FOR THE YEAR ENDED JUNE 30, 2004**

**Note 1 - Purpose of the Schedule and Significant Accounting Policies**

**Basis of Presentation** – OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, requires a Schedule of Expenditures of Federal Awards showing each federal financial assistance program as identified in the *Catalog of Federal Domestic Assistance*. The accompanying schedule includes all federal grant activity for the Transportation Cabinet, except those programs administered by state universities, and is presented primarily on the basis of cash disbursements as modified by the application of KRS 45.229. Consequently, certain expenditures are recorded in the accounts only when cash is disbursed. The Commonwealth elected to exclude state universities from the statewide single audit, except as part of the audit of the basic financial statements.

KRS 45.229 provides that the Finance and Administration Cabinet may, “for a period of thirty (30) days after the close of any fiscal year, draw warrants against the available balances of appropriations made for that fiscal year, for the payment of expenditures incurred during that year or in fulfillment of contracts properly made during the year, but for no other purpose.” However, there is an exception to the application of KRS 45.229 in that regular payroll expenses incurred during the last pay period of the fiscal year are charged to the next year.

The basic financial statements of the Commonwealth are presented on the modified accrual basis of accounting for the governmental fund financial statements and the accrual basis of accounting for the government-wide, proprietary fund, and fiduciary fund financial statements. Therefore, the schedule may not be directly traceable to the basic financial statements in all cases.

Noncash assistance programs are not reported in the basic financial statements of the Commonwealth for FY 04. The noncash expenditures, where applicable, presented on this schedule represent the noncash assistance expended.

Clusters of programs are indicated in the schedule by light gray shading.

**Inter-agency Activity** - Certain transactions relating to federal financial assistance may appear in the records of more than one (1) state agency. To avoid the overstatement of federal expenditures, the following policies were adopted for the presentation of the schedule:

- (a) Federal moneys may be received by a state agency and passed through to another state agency where the moneys are expended. Except for pass-throughs to state universities as discussed below, this inter-agency transfer activity is reported by the agency expending the moneys.

State agencies that pass federal funds to state universities report those amounts as expenditures.

**NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS**  
**FOR THE YEAR ENDED JUNE 30, 2004**

**Note 1 - Purpose of the Schedule and Significant Accounting Policies (Continued)**

**Inter-agency Activity**

- (b) Federal moneys received by a state agency and used to purchase goods or services from another state agency are reported in the schedule as an expenditure by the purchasing agency only.

**Note 2 - Type A Programs**

Type A programs for the Commonwealth mean any program for which total expenditures of federal awards exceeded \$20 million for FY 04. The Transportation Cabinet had the following program that met the Type A program definition for FY 04. The Commonwealth identified clusters among the Type A programs by gray shading. The Type A program and cluster was:

<b>CFDA #</b>	<b>Program Title</b>	<b>Expenditures</b>
<b>Highway Planning and Construction Cluster:</b>		
20.205	Highway Planning and Construction	\$ 466,540,160

**Note 3 - Highway Planning and Construction (CFDA #20.205)**

The information reported for this program represents the activity of all open projects during FY 04. These projects were funded from several apportionments. Apportionments refer to a federal, statutorily prescribed division or assignment of funds. The expenditures reflected on the schedule include expenditures for advance construction projects, which are not yet under agreements with the Federal Highway Administration (FHWA).

Program Income - The Highway Planning and Construction Program earned program income of \$456,068 in FY 04. This income was earned in the right-of-way phase through the sale and rental of real property. Income earned in this manner was classified as a negative expenditure, resulting in a reduction to federal expenditures for the current year.

Refunds - Expenditures for the Highway Planning and Construction Program were shown net of any refunds, resulting from a reimbursement of prior or current year expenditures. Refunds totaled \$1,631,354 for FY 04.

**FINANCIAL STATEMENT FINDINGS*****Reportable Conditions Relating to Internal Controls and/or  
Reportable Instances of Noncompliance*****FINDING 04-TC-1: The Transportation Cabinet Should Improve Inventory Procedures For Maintenance Materials**

---

The Transportation Cabinet (TC) has maintenance barns in each of the 12 districts throughout Kentucky. For FY 04, TC had \$25.3 million worth of inventory on their balance sheet. Our auditors observed district personnel conduct their inventory to determine if maintenance materials were counted correctly and to determine if inventory management procedures were adequate.

Several inconsistencies were noted. Some sites had complete guardrail systems on their lot and did not count them with their inventory, while others did. These guardrail systems appear to be leftovers from construction projects. In 4 counties we observed, the guardrail systems and remnants totaled approximately \$5,775.

Items such as antifreeze, oil, grease, etc were included on the OMS inventory sheets used by district personnel in conducting their inventory. District personnel were unclear as to whether they were responsible for counting those items or not because those are usually included with the Equipment Division inventory. In the 4 counties observed, items such as antifreeze, oil and grease totaled \$3,756.

There were several instances where the observers had written in additions on the OMS inventory sheets, however, these additions were not made by the record keepers.

There are no policies and procedures in place to instruct district maintenance personnel on inventory procedures. Record keepers do not have a clear understanding of OMS and have not been adequately trained.

Statement 1, paragraph 73 of the National Council of Governmental Accounting (NCGA) requires "significant amounts of governmental fund inventories to be reported in the fund balance sheet." Such a requirement makes it imperative to have accurate counts of inventory.

**Recommendation**

We recommend TC develop policies and procedures for inventory observations. These policies and procedures should cover items such as what to do with leftover construction project materials as well as responsibilities of each division. Record keepers should be adequately trained on using the OMS system. There were several new timekeepers who expressed their desire and need for OMS training.

**FINANCIAL STATEMENT FINDINGS*****Reportable Conditions Relating to Internal Controls and/or  
Reportable Instances of Noncompliance*****FINDING 04-TC-1: The Transportation Cabinet Should Improve Inventory  
Procedures For Maintenance Materials (Continued)**

---

**Management Response and Corrective Action Plan**

*The Kentucky Transportation Cabinet (TC) has developed a Policies and Procedures manual for OMS Material inventory and for inventory observations. This manual was revised and updated in March 2005. While each inventory item is not specifically mentioned, there is a policy outlined for all materials in the inventory. This includes salvaged guardrail components and items received from the Equipment garages or the central office Equipment Warehouse. The revised manuals are being sent to each district for distribution to all administrative units. In response to training needs, when the OMS system was implemented, all OMS administrative units were given extensive training. The OMS training team is committed to providing training to any administrative unit requesting training. We feel the procedures in place during the inventory process were meeting the objective of National Council of Governmental Accounting criteria requiring "significant amounts of governmental fund inventories to be reported in the fund balance sheet.*

**FINANCIAL STATEMENT FINDINGS*****Reportable Conditions Relating to Internal Controls and/or  
Reportable Instances of Noncompliance*****FINDING 04-TC-2: The Transportation Cabinet Should Implement Procedures To  
Ensure An Accurate Conversion Of Data To New Systems**

---

The Department of Bridge Inspections maintains its information in two (2) separate software programs located on two (2) different servers. The authoritative source for bridge information is the National Bridge Information System (NBIS), which is housed on a mainframe computer. However, the department also maintains its own data in the Kentucky Bridge Information System (KBIS), which is in development and is housed on a Windows NT server. Per discussion with TC management, this is only temporary; eventually, KBIS will become the authoritative source for bridge information.

This type of situation increases the possibility for errors and discrepancies.

During the process of developing and implementing a new system that is replacing a current system, procedures should be established to ensure the complete and accurate conversion of current system data to the new system.

**Recommendation**

We recommend that department management ensure KBIS implementation procedures include a procedure to perform a thorough comparison of all data in NBIS and KBIS to ensure the completeness and accuracy of data housed within the new KBIS system.

**Management Response and Corrective Action Plan****FY 03 Response:**

*The Division of Operations Bridge Inspection Section still maintains its information in two separate software programs the National Bridge Information System (NBIS) that is housed on a mainframe computer, and the Kentucky Bridge Information System (KBIS) that is housed on a Windows 2000 server. This is only being done temporarily and that eventually KBIS will become the authoritative source for bridge information. During this temporary stage, which is almost final stage, we have always been successful in making sure no errors occur. We are making sure of the completeness and accuracy of bridge inspection and inventory data during on-going collection and input activities. We are hoping by July 2004 the KBIS will be implemented, and the KBIS will be part of Kentucky Bridge*

*Maintenance system (KYBMS) software in future so that NBIS that resides on the mainframe will no longer exist.*

**FINANCIAL STATEMENT FINDINGS**

***Reportable Conditions Relating to Internal Controls and/or  
Reportable Instances of Noncompliance***

**FINDING 04-TC-2: The Transportation Cabinet Should Implement Procedures To  
Ensure An Accurate Conversion Of Data To New Systems (Continued)**

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**Management Response and Corrective Action Plan**

**FY 04 Response:**

*The Division of Operations Bridge Management Branch purchased the KYBMS system to replace the KBIS system several years ago. Both systems are being maintained until Operations personnel are assured the new system will meet the need to evaluate the status of bridges maintenance needs. This has been a slow process due mostly to employee turnover in the affected branch. Currently a new staff member has been assigned the task of evaluating and utilizing the KYBMS system.*



**FINANCIAL STATEMENT FINDINGS*****Reportable Conditions Relating to Internal Controls and/or  
Reportable Instances of Noncompliance*****FINDING 04-TC-3: The Transportation Cabinet Should Implement Procedures To  
Ensure The Integrity Of The Highway Information System Database**

---

The Highway Information System (HIS) maintains data on bridges, as well as all other public roads in the state. The information contained in the HIS database is collected and maintained by various TC divisions. The integrity of the HIS data is dependent upon both the accuracy and frequency with which the data is updated and the users interpretation. It was noted in the prior year audit that there is no time schedule for updating that data. The source of the bridge information is kept on the NBIS server. The Department of Bridge Inspections maintains this data. Per current discussion with management, we noted that it has been several months since the HIS server had downloaded the latest information from NBIS and that no new processes have been implemented to compare the data contained in the HIS server with that contained in the NBIS server.

The agency has stated this was due to a scheduled replacement of NBIS. To date, no additional procedures have been performed to ensure that HIS data has been updated from the current KBIS data. The agency expects to upgrade HIS in the first half of 2004 to actually implement a direct link to KBIS information for HIS users and eliminate the need for KBIS downloads into HIS.

When information regarding bridges is not updated periodically, the various divisions within the TC do not have the most recent information for analysis purposes. Specifically, it is important for the Division of Planning, which uses that data in HIS, to have current and reviewed information regarding bridges.

Data integrity control procedures should be established that are adequate to ensure the integrity of the data maintained within the organization's databases. Procedures should be established to ensure that data used by management remains complete, accurate and valid during its input, update, and storage. Further, data elements should be balanced periodically to the control records or master files in the case of data interfaces.

**Recommendation**

Procedures should be implemented that ensure the integrity and completeness of bridge information provided to HIS users. Until the direct link between HIS and KBIS information is completed, we recommend a current download from KBIS to HIS be performed and data be refreshed at least on a quarterly basis.

**FINANCIAL STATEMENT FINDINGS*****Reportable Conditions Relating to Internal Controls and/or  
Reportable Instances of Noncompliance*****FINDING 04-TC-3: The Transportation Cabinet Should Implement Procedures To  
Ensure The Integrity Of The Highway Information System Database (Continued)**

---

**Management Response and Corrective Action Plan****FY 03 Response:**

*We would like to re-emphasize that bridge data is maintained and available from the Traffic & Operations Division. KBIS is the official source file for reporting and/or analysis.*

*As stated last August, our goal is to establish a link between the KBIS and HIS systems. We are currently developing a process to download bridge information from KBIS, including the new unique bridge id, to the existing HIS system. As the HIS upgrade progresses, this download will assist us in our design and plan for a potential link, and will aid the Traffic & Operations Division with improving bridge locations.*

*Our schedule for upgrading the HIS system to Highways by Exor includes a production load of existing data for evaluation by June 30<sup>th</sup> of this year, and running in parallel with the current system until it is determined that the upgrade successfully meets the Cabinet's reporting and analysis requirements.*

**FY 04 Response:**

*The Division of Planning uses the Highway Information System (HIS) system to maintain the inventory of all Transportation Highway Infrastructure. To track bridges there has been an effort to link the HIS system to the Bridge Maintenance System (BMS) in order to ensure accurate tracking of all bridges. This linking of data has been delayed due to the implementation of a new HIS system (developed by Exor) which upgrades the HIS system to a new platform to accommodate the Cabinet wide enterprise system. The Division of Operations inability to implement the new KYBIS system that replaces the KBIS system (mentioned in number 3 above) also consternates the resolution of this condition.*

**FINANCIAL STATEMENT FINDINGS*****Reportable Conditions Relating to Internal Controls and/or  
Reportable Instances of Noncompliance*****FINDING 04-TC-4: The Transportation Cabinet Should Improve Data Retention Practices**

---

Our examinations of the data retention for information maintained within the NBIS and within the Pavement Management System (Visual/PMS) revealed that year-end downloads are not kept for these databases. Information contained in the Required Supplementary Information includes prior year data. Additionally, trend analysis often requires detailed information for prior year data that may not have been included in a separate report.

Failure to retain year-end downloads means there is no practical method to determine or test the records and their corresponding field data for prior years.

Electronic data that provides support for financials included within the annual report should be retained in a manner similar to that required for non-electronic support. This data should be retained as provided for in an approved retention schedule with the Kentucky Department of Library and Archives. Master files and electronic data that is considered necessary for an audit trail should be retained as long as necessary for audit purposes.

**Recommendation**

We recommend the TC ensure they retain year-end downloads for the NBIS and Visual/PMS databases in order to facilitate and substantiate prior year reporting, as well as to provide a detailed backup that can be tested for accuracy in the event clarification is needed. If upgrades to these systems have been or will be implemented, then the TC should ensure the same considerations for data retention are included in the implementation.

**Management Response and Corrective Action Plan****FY 03 Response**

*A Bridge Management System (BMS) and a Pavement Management System (PMS) have been selected for implementation, but these systems have not been fully implemented. The pavement management data and the Bridge Inventory data at present is stored on the mainframe with back-up of the data as per GOT's policy and procedures for backing up data. Data entered in the selected Visual BMS and PMS has a date/time and user stamp in the database. Therefore, the changes in the data can be tracked. All prior year data is available to do trends analysis. With the full implementation of these two systems in the next one to two years, the stated weakness will cease to exist.*

**FINANCIAL STATEMENT FINDINGS**

***Reportable Conditions Relating to Internal Controls and/or  
Reportable Instances of Noncompliance***

**FINDING 04-TC-4: The Transportation Cabinet Should Improve Data Retention Practices (Continued)**

---

**Management Response and Corrective Action Plan**

**FY 04 Response**

*The Division of Operations is still working to implement the changes detailed in the response to the auditors FY 03 finding. Operations is running dual systems at this time and with some minor computer program modifications will be ready to cut over to the new software. The target date for completion is by the end of Fiscal Year 2005. As recommended by the Auditor's Office, the new software will track data changes and the user making the changes.*

**FINANCIAL STATEMENT FINDINGS*****Reportable Conditions Relating to Internal Controls and/or  
Reportable Instances of Noncompliance*****FINDING 04-TC-5: The Transportation Cabinet Should Improve Audit Trail Procedures For Database Actions**

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Adequate audit trails were not implemented for various databases within TC. Our examination of internal controls over infrastructure assets revealed that no reports are currently generated by TC that show the data attribute changes, records added, and records deleted. In addition, some databases do not contain a field for when the date information was entered or a field identifying the user performing the data entry.

In order to properly track potential data entry errors or other errors in the database, it is important to know when the entry error occurred and the identity of the individual making the entry.

Without adequate audit trails, it is difficult or impossible to determine the exact timing, source, and cause of database data entry errors or unauthorized changes to records. It may also result in the inability to properly recover data in the case of some errors.

Adequate audit trails should be provided to facilitate the tracing of transaction processing and the reconciliation of disputed data. Accounting systems and database management systems should include an audit trail component that includes sufficient information, such as the terminal device or microcomputer involved, user identification codes, data field affected, and time and date entries. TC's system development life cycle methodology should include procedures requiring that each information system development or modification project have adequate audit trails specified.

**Recommendation**

We suggest TC consider adding fields to provide sufficient audit trails of database alterations or security violations, including the date entered and entry person for all changes to the critical databases. In addition, we believe TC should consider generating a nightly report showing all changes to the database that were made each day.

**Management Response and Corrective Action Plan****FY 03 Response**

*During analysis of the Land & Buildings database/application, new requirements were uncovered which kept increasing the scope of the project; some of the requirements also [would have] generated policy and process changes. Effectively, because of other priorities and setbacks, the effort waned. At this time, we are making a minimum number of changes to the database and system in an effort to comply with the intent of the recommendations. These changes are expected to be complete by the end of this month.*

**FINANCIAL STATEMENT FINDINGS*****Reportable Conditions Relating to Internal Controls and/or  
Reportable Instances of Noncompliance*****FINDING 04-TC-5: The Transportation Cabinet Should Improve Audit Trail  
Procedures For Database Actions (Continued)**

---

**Management Response and Corrective Action Plan**

*Further remediation efforts and/or a possible rewrite of a lands & building inventory system need to be at the direction of the system user/owner - Division of Property and Supply Services. Likewise, further responses to issues surrounding this system should likely be coordinated through the Division of Property and Supply Services.*

**FY 04 Response**

*Asset tracking for the Cabinet is achieved on 4 separate platforms. These systems are very diverse in nature and the solution offered by the auditor's office does not apply to all of these systems.*

- A) Vehicles are tracked with the OMS system and the inventory controls are an intricate part of this system. It was developed by a third party and does not contain the tracking of changes suggested by the Auditor's Office. It does a very good job of maintaining the assignment, billing and recovery of cost for the Cabinet. There are no plans at this time to modify this system to track changes to vehicle inventory.*
- B) Office & Lab Equipment is tracked using the MARS statewide system which also does not track changes to the system as outlined by the auditors.*
- C) Lots & Building are tracked using a Dbase III application. This system has just been upgraded by the Division of Technology and should fully meet the expectations of the Auditor's Office.*
- D) Computer Equipment & Software is tracked on a Dbase III application. This software doesn't address the auditor's recommendations and there are no plans to modify the application now used. It does however meet the needs of the Division of Technology for their computer tracking needs.*

*There is a preliminary study to replace systems B, C, D with a software package named Archibus. This system is an integrated package that inventories and tracks Lots, Buildings and their contents. It is currently in use by the Finance and Administration Cabinet's Real Property Section and we could possibly become a part of a statewide system.*

## FINANCIAL STATEMENT FINDINGS

### *Other Matters Relating to Internal Controls and/or Instances of Noncompliance*

#### **FINDING 04-TC-6: The Transportation Cabinet Password Policy Should Be Consistently Applied To All Local Area Network Servers**

During the security vulnerability testing for FY 04, TC did not ensure password policies established on machines adhered to the agency-established password policies. The auditor used standard scanning tools and received account related information from seven machines. This information was compared to the agency-established password policy criteria. See the table below for a summary of our findings.

Security Measure	Standard	Number of machines not in compliance with policy	Percentage of 7 machines not in compliance with policy
Maximum Age	31 days	2 – None 4 – 42 days	85.7%
Minimum Age	1 day	6 – None	85.7%
Minimum Length	8 characters	6 – None	85.7%
Lockout Threshold	3 attempts	6 – None	85.7%

If machines within a network are not sufficiently secured, the network could be compromised.

Passwords are an important aspect of computer security. They are the front line of protection for system access. To help ensure the security of a network, it is necessary for a strong password policy to be developed and implemented on all servers within the network in a consistent manner.

#### **Recommendation**

We recommend that TC review all machines within their agency-owned domains to ensure that the password policies comply with the agency-established password policy.

#### **Management Response and Corrective Action Plan**

*Two of the machines listed are not TC machines, therefore we have no control over their password rules even though they exist on our network. We have moved these machines to a separate sub-net with no access to the remainder of our network.*

*The remainder of the machines existed on an incorrect sub-net and therefore password rules were not being enforced. They have been moved to the correct sub-net.*

## **FINANCIAL STATEMENT FINDINGS**

### ***Other Matters Relating to Internal Controls and/or Instances of Noncompliance***

#### **FINDING 04-TC-7: The Transportation Cabinet Should Ensure All Accounts On Its Agency Machines Are Necessary**

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During the security vulnerability testing for FY 04 on machines controlled by TC, NetBIOS account information was received from seven machines. To determine if there are unnecessary accounts on these machines, the auditor used the criterion that the account password was over the 31-day maximum age. The auditor discovered 92 accounts that met this criterion. The passwords on these accounts had not been changed from between 80 to 1891 days. The default Administrator account had not been renamed on six of these machines.

Further, the auditor was able to gain anonymous access to shares on one machine using the guest account with blank passwords. This access allowed the ability to write to the machine and at the least could provide potential unauthorized use of the 62 gigabytes of storage. We noted nothing in the directories that would suggest a hacker was using the site but this is a critical vulnerability.

If the agency's password policy is not enforced, an unauthorized user could obtain access to the accounts established on a machine.

Intruders often use inactive accounts to break into a network. If an account has not been used for a reasonable period of time, the account should be disabled until it is needed. This minimizes the possibility that an unauthorized user will access the account. Further, default administrator, guest, and anonymous accounts in operating system and applications are some of the first accounts that an intruder will attempt to use. Therefore, they should be assigned strong passwords or, if possible, renamed or removed immediately after installation.

#### **Recommendation**

We recommend that TC take the following actions:

- Default Administrator accounts should be renamed to something more ambiguous in order to prevent unauthorized access.
- All accounts should be given a sufficiently ambiguous password.
- All accounts on network machines should be reviewed to determine whether the password has been changed within the last 31 days. These accounts should be evaluated to determine if they are still valid accounts that are required for a business-related purpose. If not, the accounts should be disabled or deleted depending on the necessity of reinstatement of the account. All accounts should be required to comply with established password policies.



**FINANCIAL STATEMENT FINDINGS*****Other Matters Relating to Internal Controls and/or Instances of Noncompliance*****FINDING 04-TC-7: The Transportation Cabinet Should Ensure All Accounts On Its Agency Machines Are Necessary (Continued)**

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**Management Response and Corrective Action Plan**

*Two of the machines listed are not KYTC'S and therefore we cannot enforce security rules. They have been moved to a separate sub-net.*

*One of the machines is intentionally not on the domain and therefore password rules not enforced due to its existence in DMZ. It Is open to the Internet as planned.*

*One of the machines is a print server controlled by a third party vendor on which we cannot set password rules.*

*The remainder of the machines have been moved to the correct sub-net and the accounts will be reviewed for compliance.*

## **FINANCIAL STATEMENT FINDINGS**

### ***Other Matters Relating to Internal Controls and/or Instances of Noncompliance***

#### **FINDING 04-TC-8: The Transportation Cabinet Should Ensure All Open Ports On Agency Machines Have A Business Related Purpose**

During the security vulnerability assessments for FY 04 for machines controlled by TC, our examination revealed that there were seven machines with ports open that may not have a specific business-related purpose. Due to the large number of issues, we grouped the findings below by port number and application.

##### **Port 7 - Echo**

One machine was identified as having port 7 open. This port is used for the Echo service, which could allow a potential Denial of Server (DoS) attack.

##### **Port 21 – FTP**

One machine was found to have port 21 open, which is used for File Transfer Protocol (FTP). The auditor was able to gain anonymous access to this machine in which we were able to view files and folders via the Internet including some application executables.

##### **Port 25 – SMTP**

One machine was found to have port 25 open, which is used for Simple Mail Transfer Protocol (SMTP). It was determined that this machine is not running the most current version of SMTP that is available. There are vulnerabilities associated with less current versions of SMTP.

##### **Port 1761 and 1763 - LANDesk**

Five machines were identified as having ports 1761 and 1763 open, which is used for the LANDesk product. The auditor has determined that the Landesk Management Suite is a systems management product, which enables administrators to automate systems management tasks and proactively control desktops, servers and mobile devices - all from a single console.

There appears to be a business necessity for these ports being open, however, they should be reviewed to ensure adequate security has been applied since this product may contain an ActiveX component that could be vulnerable to a buffer overflow attack.

##### **Port 3017 (Event Listener)**

Three machines were found to have port 3017 open, which is running the Event Listener. This port should be reviewed to ensure there is a valid business-related purpose for having it open.

##### **Port 3339 – anet-1**

One machine was found to have port 3339 open. This port should be reviewed to ensure there is a valid business-related purpose for having it open.

## **FINANCIAL STATEMENT FINDINGS**

### ***Other Matters Relating to Internal Controls and/or Instances of Noncompliance***

#### **FINDING 04-TC-8: The Transportation Cabinet Should Ensure All Open Ports On Agency Machines Have A Business Related Purpose (Continued)**

##### **Port 3339 – anet-1**

One machine was found to have port 3339 open. This port should be reviewed to ensure there is a valid business-related purpose for having it open.

##### **Port 5631 (pcanywhere)**

One machine was found to have port 5631 open. This port should be reviewed to ensure there is a valid business-related purpose for having it open.

##### **Port 13722 – bpjava-msvc**

One machine was found to have port 13722 open, which is set up as the BP Java MSVC Protocol. This port appears to be used by the Veritas NetBackup product; however, a specific use could not be determined. This port should be reviewed to ensure there is a valid business-related purpose for having it open.

##### **Port 49400 – compaqdiag**

One machine was found to have port 49400 open, which is used for the Compaqdiag service. This port could be vulnerable to the Cross Site Scripting vulnerability (XSS).

The auditor could not determine the necessity of some of these ports being open. Some, however, appear to be vital in order for TC to conduct business. Therefore, the agency should review these ports to ensure they have a business-related purpose. If they are required, then the proper security measures should be taken to protect them from vulnerability.

Intruders could obtain access to a system through an open port if proper security measures are not applied.

The existence of open ports is an invitation for intruders to enter your system. To minimize the risk of unauthorized access to a machine, only necessary, business-related ports should be open. Further, the application residing at these ports should be secured to the extent possible.

#### **Recommendation**

We recommend that TC review all open ports to ensure there is a specific business-related purpose requiring the port to be open. If not required, then that port should be closed. If the port is necessary, then TC should ensure adequate logical security controls are implemented to prevent unauthorized access.

**FINANCIAL STATEMENT FINDINGS*****Other Matters Relating to Internal Controls and/or Instances of Noncompliance*****FINDING 04-TC-8: The Transportation Cabinet Should Ensure All Open Ports On Agency Machines Have A Business Related Purpose (Continued)**

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**Management Response and Corrective Action Plan**

*Port 7 - This is on a telephone switch. Our network staff will review.*

*Port 21- We have a valid business need (FTP) for this port to be open.*

*Port 25- This open port has been removed.*

*Ports 1761 & 1763 – Upon review it was determined that there was a valid business need for these ports to be open, however they had unnecessary exposure due to their placement on the network. They were subsequently moved.*

*Port 3017- – Upon review it was determined that there was a valid business need for this port to be open, however they had unnecessary exposure due to their placement on the network. They were subsequently moved.*

*Port 3339- We will be reviewing the reason for this port being open.*

*Port 5631- We have a valid business need (PCAnywhere) for this port to be open.*

*Port 13722 - We have a valid business need (NetBackup) for this port to be open.*

*Port 49400 - We have a valid business need for this port to be open.*

**FEDERAL AWARD FINDINGS AND QUESTIONED COST*****Reportable Conditions Relating to Internal Control and/or  
Reportable Instances of Noncompliance*****FINDING 04-TC-9: The Transportation Cabinet Should Improve The Change Order Process**

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State Agency: Transportation Cabinet

Federal Program: 20.205 – Highway Planning and Construction

Federal Agency: Not Applicable

Pass-Through Agency: U.S. Department of Transportation

Compliance Area: Allowable Costs/Cost Principles

Amount of Questioned Cost: None

During our audit of TC, a draft report prepared by the Cabinet's Office of Inspector General (OIG) heightened our awareness of a situation present within the cabinet. Within this report, it was disclosed that Cabinet policies in regards to change orders were "blatantly ignored." None of the five projects mentioned within the report involved federal funds; however, if Federal Funds had been utilized, questioned cost may have arisen for these expenditures.

Our audit of the Highway Planning and Construction program noted that a total of 16 change orders were observed for one project during FY 04. Within the project file, a total of 38 change orders were observed. Numbering of change orders suggest that as many as 48 were processed over the life of the project, which appears to be excessive. During our audit, it was observed that a total of thirteen projects originally awarded a total of \$214.8 million were increased by \$12.5 million in change orders.

The Cabinet OIG disclosed that 1087 change orders were approved during FY 04.

Allowing use of multiple change orders during projects demonstrates that there is inefficient planning conducted and allows the Commonwealth to be susceptible to instances of bid-rigging and instances of fraud.

OMB Circular A-133 Part 6 states, "The A-102 Common Rule and OMB Circular A-110 require that non-Federal entities receiving Federal awards (i.e., auditee management) establish and maintain internal control designed to reasonably ensure compliance with Federal laws, regulations, and program compliance requirements."

## FEDERAL AWARD FINDINGS AND QUESTIONED COST

### *Reportable Conditions Relating to Internal Control and/or Reportable Instances of Noncompliance*

#### FINDING 04-TC-9: The Transportation Cabinet Should Improve The Change Order Process (Continued)

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##### Recommendation

The APA noted during our review of the draft report of the OIG preliminary recommendations which should be considered for implementation. Some of them are:

- “More oversight given in the use of Change orders...”
- “The use of Lump Sum Change Orders should be avoided and used only in extreme circumstances...”
- “Existing and future policy set in place to govern Change orders must be strictly enforced...”
- “Contractors who are awarded bid contracts should be, if at all possible, held to their original winning bid...”
- “ If major Change Orders address the Design of a project, the Design Division should have input as to the necessity of the change, and should be included in the approval process...”
- disagreements “should be noted by Memorandum, and attached to the Change order before it proceeds to next level...”

In addition, we recommend that:

- The Cabinet consider adopting new policies for design and planning that could possibly extinguish, or significantly reduce the use of change orders. Hold contractors to original winning bid as suggested by the Cabinet OIG.

##### Management Response and Corrective Action Plan

*The Transportation Cabinet recognizes the need for a system that maintains internal controls and compliance with all Federal and State laws, regulations and program compliance requirements. The Cabinet is currently implementing new contract management software (Transport; Site Manager), which was developed by the American Association of State Highway & Transportation Officials (AASHTO) and has been customized for Kentucky needs. This software will be fully implemented by June 30, 2005.*

*Specific responses to items in the recommendation are:*

- *"More oversight given in the use of Change orders..." **The Cabinet has increased the scrutiny of all change orders.***
- *"The use of Lump Sum Change Orders should be avoided and used only in extreme circumstances..." **Lump sum change orders are used sparingly and detailed records are maintained.***

**FEDERAL AWARD FINDINGS AND QUESTIONED COST*****Reportable Conditions Relating to Internal Control and/or  
Reportable Instances of Noncompliance*****FINDING 04-TC-9: The Transportation Cabinet Should Improve The Change Order Process (Continued)**

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**Management Response and Corrective Action Plan**

- *"Existing and future policy set in place to govern Change orders must be strictly enforced..." **The existing policy is being strictly enforced.***
- *"Contractors who are awarded bid contracts should be, if at all possible, held to their original winning bid..." **While not always possible every effort is made to limit the number of change orders.***
- *" If major Change Orders address the Design of a project, the Design Division should have input as to the necessity of the change, and should be included in the approval process..." **This policy has been in place for approximately three years.***
- *disagreements "should be noted by Memorandum, and attached to the Change order before it proceeds to next level..." **SiteManager will allow comments to become part of the change order record.***
- *The Cabinet should consider adopting new policies for design and planning that could possibly extinguish, or significantly reduce the use of change orders. **This is already in place with our "Lessons Learned Database"***
- *Hold contractors to original winning bid as suggested by the Cabinet OIG. **While not always possible every effort is made to limit the number of change orders.***

*With the implementation of the new software, Construction employees have received countless hours of training that will further strengthen the staff's ability to follow the procedures to ensure full compliance with necessary audit requirements.*

**FEDERAL AWARD FINDINGS AND QUESTIONED COST*****Reportable Conditions Relating to Internal Control and/or  
Reportable Instances of Noncompliance*****FINDING 04-TC-10: The Transportation Cabinet Should Improve Procedures To  
Ensure Federal Reports Are Submitted Timely**

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State Agency: Transportation Cabinet

Federal Program: 20.500 and 20.509 – Federal Transit – Formula Grants; Formula Grants  
for Other Than Urbanized Areas

Federal Agency: U. S. Department of Transportation

Pass-Through Agency: Not Applicable

Compliance Area: Reporting

Amount of Questioned Cost: None

OMB Circular A-110 subpart C section .52(a)(1)(i) states “Each Federal awarding agency shall require recipients to use the SF269 or SF269A to report the status of funds for all non-construction projects or programs.” During our audit of TC, thirty federal financial status reports were reviewed for timely submission. Out of the thirty reports reviewed, sixteen were submitted between five and forty days late.

Lack of compliance with the required submission dates could result in federal assistance being reduced or possibly suspended.

OMB Circular A-110 subpart C section .52 states, “(iv) The Federal awarding agency shall require recipients to submit the SF-269 or SF-269A (an original and no more than two copies) no later than 30 days after the end of each specified reporting period for quarterly and semi-annual reports, and 90 calendar days for annual and final reports. Extensions of reporting due dates may be approved by the Federal awarding agency upon request of the recipient.”

**Recommendation**

TC should strive to submit Federal Financial Status Reports within the deadlines or make formal written requests for extensions.

**Management Response and Corrective Action Plan**

*During the audit review, the auditor requested a federal time extension for the SF 269 reports with late submissions (July 2003-March 2004).*

*Please note that the Federal Transit Administration (FTA) accepted the reports with the submittal dates and the Transportation Cabinet was not cited for non-compliance with reporting requirements. The federal acceptance indicates no ramifications nor did it cause a reduction in funding.*



**FEDERAL AWARD FINDINGS AND QUESTIONED COST*****Reportable Conditions Relating to Internal Control and/or  
Reportable Instances of Noncompliance*****FINDING 04-TC-10: The Transportation Cabinet Should Improve Procedures To  
Ensure Federal Reports Are Submitted Timely (Continued)**

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**Management Response and Corrective Action Plan**

*However, to get an official statement for the Auditor, staff from the Office of Transportation Delivery called and e-mailed the federal project and requested an extension by e-mail granted the extension for said reports.*

*As a follow-up, the auditor contacted the Federal Manager and requested further information and the following is the response from the Federal Transit Administration:*

*"I am a Program Manager within the Division of Operations and Program Management in the Regional FTA Office. With regard to your questions, unless the grantee is a flagrant violator of FTA requirements, FTA will not penalize the grantee for being late in submitting their reports. Normally, we would call or send out letters reminding the grantee that their reports are past due. For flagrant violators there is a possibility that the grant would be closed if the situation does not improve."*

*The SF 269 process:*

*Before you can initiate a grant, a SF 269 report is required. Yet no activity has occurred. To expedite a grant closeout, FTA has accepted the quarterly expenditures along with the final payment the first month following the end of the quarter. This allows for a four month closeout period rather than waiting and having a six month closeout. Therefore, giving a late SF 269-report submission but having an early grant closeout. Additionally, after the final draw down, the FTA Federal Manager can closeout the grant before the State has an opportunity to submit a SF 269 report. This is because FTA can see all of the activities in the federal system along with the financial draws made from the Washington Bank to the respective project.*

*However, since the Jan-March 2004 quarterly report submissions, the staff of the Office of Transportation Delivery has submitted all reports within the thirty-day recommendation and the schedule is as follows:*

## FEDERAL AWARD FINDINGS AND QUESTIONED COST

### *Reportable Conditions Relating to Internal Control and/or Reportable Instances of Noncompliance*

#### **FINDING 04-TC-10: The Transportation Cabinet Should Improve Procedures To Ensure Federal Reports Are Submitted Timely (Continued)**

#### **Management Response and Corrective Action Plan**

*SF 269 Reports*

*Quarterly Schedule*

*TC/Office of Transportation Delivery*

<i>Grant</i>	<i>Grant #</i>	<i>FFY</i>	<i>SFY</i>	<i>Calendar</i>		<i>QTR</i>	<i>Date</i>	<i>Date</i>
				<i>Year</i>	<i>Month</i>	<i>FFY</i>	<i>Due</i>	<i>Submitted</i>
<i>KY-03</i>	<i>0046</i>	<i>05</i>	<i>05</i>	<i>2004</i>	<i>October-December</i>	<i>1st</i>	<i>1/30/05</i>	<i>1/25/2005</i>
<i>KY-03</i>	<i>0050</i>	<i>05</i>	<i>05</i>	<i>2004</i>	<i>October-December</i>	<i>1st</i>	<i>1/30/05</i>	<i>1/26/2005</i>
<i>KY-03</i>	<i>0054</i>	<i>05</i>	<i>05</i>	<i>2004</i>	<i>October-December</i>	<i>1st</i>	<i>1/30/05</i>	<i>1/26/2005</i>
<i>KY-03</i>	<i>0063</i>	<i>05</i>	<i>05</i>	<i>2004</i>	<i>October-December</i>	<i>1st</i>	<i>1/30/05</i>	<i>1/26/2005</i>
<i>KY-03</i>	<i>0066</i>	<i>05</i>	<i>05</i>	<i>2004</i>	<i>October-December</i>	<i>1st</i>	<i>1/30/05</i>	<i>1/4/2005</i>
<i>KY-16</i>	<i>0031</i>	<i>05</i>	<i>05</i>	<i>2004</i>	<i>October-December</i>	<i>1st</i>	<i>1/30/05</i>	<i>1/28/2005</i>
<i>KY-18</i>	<i>0022</i>	<i>05</i>	<i>05</i>	<i>2004</i>	<i>October-December</i>	<i>1st</i>	<i>1/30/05</i>	<i>1/28/2005</i>
<i>KY080</i>	<i>X12</i>	<i>05</i>	<i>05</i>	<i>2004</i>	<i>October-December</i>	<i>1st</i>	<i>1/30/05</i>	<i>1/28/2005</i>
<i>KY080</i>	<i>X13</i>	<i>05</i>	<i>05</i>	<i>2004</i>	<i>October-December</i>	<i>1st</i>	<i>1/30/05</i>	<i>1/28/2005</i>
<i>KY-03</i>	<i>0046</i>	<i>04</i>	<i>05</i>	<i>2004</i>	<i>July-September</i>	<i>4th</i>	<i>10/30/05</i>	<i>10/25/2004</i>
<i>KY-03</i>	<i>0054</i>	<i>04</i>	<i>05</i>	<i>2004</i>	<i>July-September</i>	<i>4th</i>	<i>10/30/05</i>	<i>10/25/2004</i>
<i>KY-16</i>	<i>0031</i>	<i>04</i>	<i>05</i>	<i>2004</i>	<i>July-September</i>	<i>4th</i>	<i>10/30/05</i>	<i>10/27/2004</i>
<i>KY-18</i>	<i>0021</i>	<i>04</i>	<i>05</i>	<i>2004</i>	<i>July-September</i>	<i>4th</i>	<i>10/30/05</i>	<i>10/27/2004</i>
<i>KY-18</i>	<i>0022</i>	<i>04</i>	<i>05</i>	<i>2004</i>	<i>July-September</i>	<i>4th</i>	<i>10/30/05</i>	<i>10/27/2004</i>
<i>KY-90</i>	<i>X138</i>	<i>04</i>	<i>05</i>	<i>2004</i>	<i>July-September</i>	<i>4th</i>	<i>10/30/05</i>	<i>10/27/2004</i>
<i>KY-90</i>	<i>X140</i>	<i>04</i>	<i>05</i>	<i>2004</i>	<i>July-September</i>	<i>4th</i>	<i>10/30/05</i>	<i>10/27/2004</i>
<i>KY080</i>	<i>X11</i>	<i>04</i>	<i>05</i>	<i>2004</i>	<i>July-September</i>	<i>4th</i>	<i>10/30/05</i>	<i>10/29/2004</i>
<i>KY080</i>	<i>X12</i>	<i>04</i>	<i>05</i>	<i>2004</i>	<i>July-September</i>	<i>4th</i>	<i>10/30/05</i>	<i>10/27/2004</i>
<i>KY-03</i>	<i>0038</i>	<i>04</i>	<i>04</i>	<i>2004</i>	<i>April-June</i>	<i>3rd</i>	<i>7/30/04</i>	<i>7/8/2004</i>
<i>KY-03</i>	<i>0046</i>	<i>04</i>	<i>04</i>	<i>2004</i>	<i>April-June</i>	<i>3rd</i>	<i>7/30/04</i>	<i>7/8/2004</i>
<i>KY-03</i>	<i>0047</i>	<i>04</i>	<i>04</i>	<i>2004</i>	<i>April-June</i>	<i>3rd</i>	<i>7/30/04</i>	<i>7/8/2004</i>
<i>KY-03</i>	<i>0048</i>	<i>04</i>	<i>04</i>	<i>2004</i>	<i>April-June</i>	<i>3rd</i>	<i>7/30/04</i>	<i>7/8/2004</i>
<i>KY-03</i>	<i>0050</i>	<i>04</i>	<i>04</i>	<i>2004</i>	<i>April-June</i>	<i>3rd</i>	<i>7/30/04</i>	<i>7/26/2004</i>
<i>KY-03</i>	<i>0054</i>	<i>04</i>	<i>04</i>	<i>2004</i>	<i>April-June</i>	<i>3rd</i>	<i>7/30/04</i>	<i>7/26/2004</i>
<i>KY-16</i>	<i>0030</i>	<i>04</i>	<i>04</i>	<i>2004</i>	<i>April-June</i>	<i>3rd</i>	<i>7/30/04</i>	<i>7/26/2004</i>
<i>KY-16</i>	<i>0031</i>	<i>04</i>	<i>04</i>	<i>2004</i>	<i>April-June</i>	<i>3rd</i>	<i>7/30/04</i>	<i>7/26/2004</i>
<i>KY-90</i>	<i>X138</i>	<i>04</i>	<i>04</i>	<i>2004</i>	<i>April-June</i>	<i>3rd</i>	<i>7/30/04</i>	<i>7/26/2004</i>
<i>KY080</i>	<i>X11</i>	<i>04</i>	<i>04</i>	<i>2004</i>	<i>April-June</i>	<i>3rd</i>	<i>7/30/04</i>	<i>7/26/2004</i>
<i>KY080</i>	<i>X12</i>	<i>04</i>	<i>04</i>	<i>2004</i>	<i>April-June</i>	<i>3rd</i>	<i>7/30/04</i>	<i>7/26/2004</i>
<i>KY-18</i>	<i>0021</i>	<i>04</i>	<i>04</i>	<i>2004</i>	<i>April-June</i>	<i>3rd</i>	<i>7/30/04</i>	<i>7/26/2004</i>
<i>KY-18</i>	<i>0022</i>	<i>04</i>	<i>04</i>	<i>2004</i>	<i>April-June</i>	<i>3rd</i>	<i>7/30/04</i>	<i>7/26/2004</i>

**FEDERAL AWARD FINDINGS AND QUESTIONED COST**

***Reportable Conditions Relating to Internal Control and/or  
Reportable Instances of Noncompliance***

**FINDING 04-TC-10: The Transportation Cabinet Should Improve Procedures To Ensure  
Federal Reports Are Submitted Timely (Continued)**

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**Management Response and Corrective Action Plan**

*If you follow the strict thirty day period submission and a grant nears closeout, the grant closeout could be delayed and the FTA Manager may initiate closeout on the federal side.*

*In summation, the Office of Transportation Delivery staff shall continue to submit the Federal Financial Status Reports within the deadlines or make a formal request for extension in order to expedite grant closeouts. The reports will be electronically submitted by the Staff Assistant and the Administrative Specialist III will maintain the schedule denoting the submittal dates.*

**FEDERAL AWARD FINDINGS AND QUESTIONED COST*****Reportable Conditions Relating to Internal Control and/or  
Reportable Instances of Noncompliance*****FINDING 04-TC-11: The Transportation Cabinet Should Improve Procedures To  
Ensure Federal Reports Are Prepared Accurately**

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State Agency: Transportation Cabinet

Federal Program: 20.205 - Highway Planning and Construction

Federal Agency: U.S. Department of Transportation

Pass-Through Agency: Not Applicable

Compliance Area: Reporting

Amount of Questioned Cost: None

TC is responsible for submitting an "Office of Real Estate Services Annual Program Statistics" to the regional Federal Highway Administration (FHWA) each federal fiscal year. We tested the FY 04 Report and found several discrepancies. There were numerous totals on the report that did not agree to supporting documentation. These were not major discrepancies, however, they were not accurate. This report is often times electronic, however, this year, FHWA did not provide an electronic version. TC simply submitted a handwritten report to FHWA with no transmittal letter. The report submitted lacked the Division, Date of Report and reporting period. Auditor had to contact the FHWA to determine when the report was submitted. We also found that amounts recorded within the report were inaccurate.

Great improvements have been made by the Division of Right of Way and Utilities with this report. Recommendations from our FY 03 audit have been put in place accordance with TC's corrective action plan. However, it appears that an in-depth review of this report is not being performed by management.

49 CFR subpart 24, Appendix B states "Submit an original and two copies of this report to (Name and Address of Federal Agency) as soon as possible after September 30, but NOT LATER THAN NOVEMBER 15." This report was not submitted until January 10, 2005, which is 3 months late.

**Recommendation**

We recommend the Division of Right of Way and Utilities develop policies and procedures for checking figures reported in the Statistical Report. We also recommend that the report be complete, accurate, reviewed and accompanied by a transmittal letter or dated report.

**FEDERAL AWARD FINDINGS AND QUESTIONED COST*****Reportable Conditions Relating to Internal Control and/or  
Reportable Instances of Noncompliance*****FINDING 04-TC-11: The Transportation Cabinet Should Improve Procedures To  
Ensure Federal Reports are Prepared Accurately (Continued)**

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**Management Response and Corrective Action Plan**

*A system of codes similar to the one now implemented in the Relocation Branch has been developed for the Acquisition Branch. These codes will be used in the Reporting Category of the MARS funding strip to identify the type of payment being made. This should allow for easier reconciliation of the MARS data and the in house records. This will also help identify any keying errors and enable a correction to be made through a JVB to ensure more accurate reporting. At the suggestion of your office, the Relocation Branch is submitting a revised report. The Division is also in the process of amending it's policy and procedures to reflect an administrative review and timely filing of the annual report.*

**FEDERAL AWARD FINDINGS AND QUESTIONED COST*****Reportable Conditions Relating to Internal Control and/or  
Reportable Instances of Noncompliance*****FINDING 04-TC-12: The Transportation Cabinet Should Improve Review And Authorization Procedures For Relocation Payments**

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State Agency: Transportation Cabinet

Federal Program 20.205 – Highway Planning and Construction

Federal Agency: U.S. Department of Transportation

Pass-Through Agency: Not Applicable

Compliance Area: Allowable Costs/Cost Principles; Special Tests & Provisions

Amount of Questioned Cost: None

During our audit testing of relocation expenditures we found that procedures are inadequate to ensure that 'Payment Summaries' are authorized by signature of a central office supervisor prior to payment being made to displacees. Specifically, in thirty-five Relocation expenditures examined, a payment of \$1,000 was made to a displacee without first obtaining a signature of a central office supervisor on the 'Payment Summary' to authorize the payment

Without proper review and authorization of Relocation payments, disbursement may be made for costs or activities that are unallowed for the Highway Planning and Construction program.

OMB Circular A-133 Part 6 states, "The A-102 Common Rule and OMB Circular A-110 require that non-Federal entities receiving Federal awards (i.e., auditee management) establish and maintain internal control designed to reasonably ensure compliance with Federal laws, regulations, and program compliance requirements."

An adequate internal control system over disbursements requires that payments be reviewed and authorized by appropriate personnel.

**Recommendation**

The Right of Way Division should remind supervisors and employees initiating or processing payments to be sure that all applicable signatures or approvals have been obtained and documented in accordance with the Division's procedures prior to disbursement of funds, reducing the likelihood of the disbursement of funds for costs or activities unallowed.

**Management Response and Corrective Action Plan**

*The unapproved relocation payment at Central Office level was an oversight. The payment was for a fixed rate move and all documentation was included in the packet. A reminder will be sent to all appropriate personnel regarding the payment approval procedure.*

**FEDERAL AWARD FINDINGS AND QUESTIONED COST*****Reportable Conditions Relating to Internal Control and/or  
Reportable Instances of Noncompliance*****FINDING 04-TC-13: The Transportation Cabinet Should Ensure FWHHA Approval Is  
Obtained Before Relocation Payments Are Made**

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State Agency: Transportation Cabinet

Federal Program: 20.205 – Highway Planning and Construction

Federal Agency: U.S. Department of Transportation

Pass-Through Agency: Not Applicable

Compliance Area: Special Tests and Provisions

Amount of Questioned Cost: \$65,129.38

During our testing of relocation expenditures, we found that there were inadequate procedures in place to ensure that the Federal Highway Administration authorized relocation expenditures on the project agreement (Form PR-1) before relocation payments were made. We found two instances, out of 35 items tested, where relocation expenditures were charged to the federal project, but the project agreement stated that 'No Relocation' payments were authorized. Relocation expenditures totaling \$65,129.38 were charged to these two acquisition projects.

Lack of compliance with conditions contained in the project agreement could cause a reduction or suspension of federal assistance.

The A-133 Compliance Supplement states, "Federal funds can be used only to reimburse costs that are in accordance with the conditions contained in the project agreement and the plans, specifications, and estimates" (23 CFR sections 1.9, 630.106 and 630.205).

**Recommendation**

The Division of Right of Way should remind supervisors and employees initiating or processing payments to be sure that relocation expenditures have been authorized by the FHWA. We recommend that the employee confirm relocation expenditures are in compliance with the project agreement and, if not agreeable, then the employee should inform the Division Director that a request for a redirection of funds is needed.

**Management Response and Corrective Action Plan**

1. *Met with all parties involved including District and Central Office Staff.*
2. *Will advise all Right of Way Supervisors by memo to make sure that when relocation is added to a project (that did not originally have relocation), a request will be made to central office programming to add relocation funds.*
3. *Right of Way programming will provide the Relocation Branch with a copy of the PR-1 at the time of right of way authorization on all projects. This will allow for the Relocation Branch to "double check" for relocation funding.*

**SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS**  
**FOR THE YEAR ENDED JUNE 30, 2004**

<b>Fiscal Year</b>	<b>Finding Number</b>	<b>Finding</b>	<b>CFDA Number</b>	<b>Questioned Costs</b>	<b>Comments</b>
<b><u>Reportable Conditions</u></b>					
<b><i>(1) Audit Findings that have been fully corrected:</i></b>					
FY 03	03-TC-01	The Transportation Cabinet Should Ensure Adequate Network Level Security Procedures Are Implemented	N/A	0	All issues were cleared during FY 04.
FY 03	03-TC-02	The Transportation Cabinet Should Strengthen The Logical Security Controls Over The Operations Management System	N/A	0	OMS users are not required to change their initial default password when first logging into the system; however, the default password has been changed to a more complex syntax. Comment will be downgraded to a verbal for FY 04.
FY 03	03-TC-8	The Transportation Cabinet Should Improve Inventory Procedures For Fleet Management	N/A	0	Resolved in FY 04
FY 03	03-TC-11	The Transportation Cabinet Should Obtain Proper Federal Highway Administration Approval Prior To Starting Eligible Federal Assistance Projects	20.205	0	Resolved in FY 04
FY 02	02-TC-05	The Transportation Cabinet Should Obtain Federal Highway Administration Approvals Prior To Granting Authority To Advertise For Projects	20.205	0	Corrective Action Plan does not take effect until FY 05
<b><i>(2) Audit findings not corrected or partially corrected:</i></b>					
FY 02	02-TC-02	The Transportation Cabinet Should Develop Internal Controls To Ensure Accurate Presentation Of the Annual Federal Highway Administration Statistics Report	20.205	0	See 04-TC-11
FY 02	02-TC-03	The Transportation Cabinet Should Ensure The Annual Federal Highway Administration Report is Compiled In Compliance With Federal Guidelines	20.205	0	See 04-TC-11



**SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS**  
**FOR THE YEAR ENDED JUNE 30, 2004**

<b>Fiscal Year</b>	<b>Finding Number</b>	<b>Finding</b>	<b>CFDA Number</b>	<b>Questioned Costs</b>	<b>Comments</b>
<b><u>Reportable Conditions</u></b>					
<b><i>(2) Audit findings not corrected or partially corrected: (Continued)</i></b>					
FY 03	03-TC-03	The Transportation Cabinet Should Implement Procedures To Ensure An Accurate Conversion of Data To New Systems	N/A	0	Corrective Action will not be implemented until FY 05 See 04-TC-2
FY 03	03-TC-04	The Transportation Cabinet Should Implement Procedures To Ensure The Integrity Of The Highway Information System Database	N/A	0	Corrective Action will not be implemented until FY 05 See 04-TC-3
FY 03	03-TC-05	The Transportation Cabinet Should Improve Data Retention Practices	N/A	0	Corrective Action will not be implemented until FY 05 See 04-TC-4
FY 03	03-TC-06	The Transportation Cabinet Should Improve Audit Trail Procedures For Database Actions	N/A	0	Corrective Action will not be implemented until FY 05 See 04-TC-5
FY 03	03-TC-12	The Transportation Cabinet Should Maintain Documentation That Supports Figures Reported In the Annual Federal Highway Administration Statistics Report.	20.205	0	See 04-TC-11

***(3) Corrective action taken is significantly different from corrective action previously reported:***

No findings for this section.

***(4) Audit finding is no longer valid or does not warrant further action:***

No findings for this section

**Other Matters**

***(1) Audit findings that have been fully corrected:***

FY 03	03-TC-7	The Transportation Cabinet Should Ensure That Staff Adhere To Agency Policies And Procedures Regarding Proper Authorization Of Expenditure Documents	N/A	0	Resolved in FY 04
FY 03	03-TC-9	The Transportation Cabinet Should Ensure Proper Useful Lives Are Being Used.	N/A	0	Resolved in FY 04

**SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS**  
**FOR THE YEAR ENDED JUNE 30, 2004**

<b>Fiscal Year</b>	<b>Finding Number</b>	<b>Finding</b>	<b>CFDA Number</b>	<b>Questioned Costs</b>	<b>Comments</b>
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**Other Matters**

*(2) Audit findings not corrected or partially corrected:*

FY 03	03-TC-13	The Transportation Cabinet Should Improve Inventory Procedures	N/ A	0	See 04-TC-01
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*(3) Corrective action taken is significantly different from corrective action previously reported:*

No findings for this section.

*(4) Audit finding is no longer valid or does not warrant further action:*

FY 03	03-TC-10	The Transportation Cabinet Should Strengthen Cash Controls	N/A	0	
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